Economic Trends

This edition of Economic Trends is taken from the *Third Quarter Fiscal Update and Economic Statement*, released on February 23, 2017.

The impact of the oil price shock on the Alberta economy appears to be subsiding. Many economic indicators are showing signs of stabilization or in the early stages of recovery, including employment, drilling and manufacturing. The economy is expected to expand in 2017, driven by oil and manufacturing exports, public sector infrastructure spending and reconstruction in Fort McMurray. The recovery in 2017, however, will be modest due to the lingering effects of low oil prices on investment and consumer spending. Real Gross Domestic Product (GDP) is forecast to grow 2.4% in 2017 (Chart 1) compared with 1.9% at *Budget 2016*. This follows a contraction of 2.8% in 2016, which was deeper than expected at *Budget 2016* due primarily to wildfire-related disruptions and lower exports.

Even as the economic recovery begins to take shape, business and household incomes, in addition to government revenue, will remain well below pre-recession levels. Nominal GDP, a broad measure of income, is forecast to improve by 5.5% this year but remain 12% below the 2014 peak.

Alberta Business Sector

Production cuts lift oil price

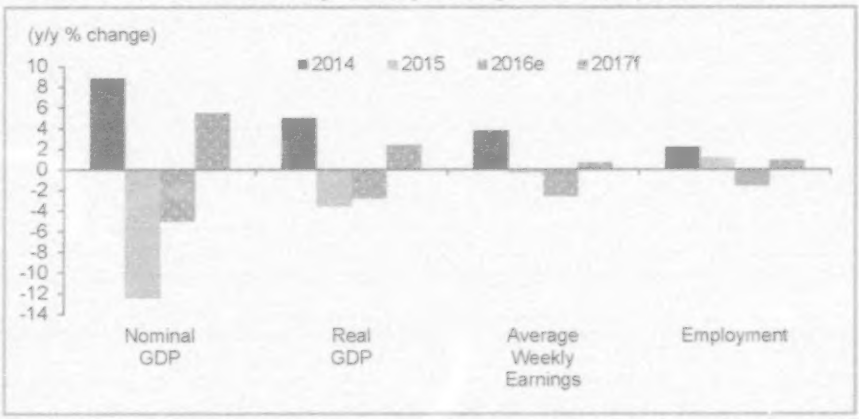
Oil prices improved in the fourth quarter of 2016 and maintained some momentum in early 2017. Prices were supported by an agreement between OPEC and major non-OPEC producers to cut oil production by almost 2 million barrels per day over the first half of 2017. This lifted oil prices above US$50/bbl. As a result, the oil price forecast for 2016-17 has been revised to US$48/bbl, up US$6/bbl from *Budget 2016*. However, elevated inventories and increasing drilling and crude oil production in the US are expected to limit price gains in 2017.

Exports surge on production

Alberta's real exports are expected to increase significantly in 2017, led by growing oil production and manufacturing. After recovering from the wildfires, Alberta's non-conventional production reached the highest level on record in late 2016. Bitumen production is forecast to increase further in 2017 as several projects come on-line. In addition, the improvement in activity in the province has boosted manufacturing, which posted broad-based increases in major categories at the end of 2016 (Chart 2). Petrochemical and petroleum product production is set to expand further in 2017. After declining by 2.0% in 2016, real exports are expected to grow by 4.4% in 2017.

Chart 1: Alberta economic indicators

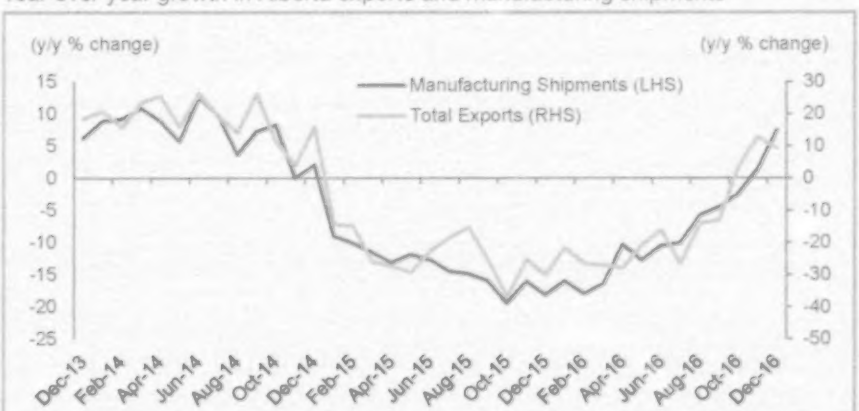
Nominal GDP, Real GDP, Average Weekly Earnings and Employment



Source: Statistics Canada, Alberta Treasury Board and Finance, e-estimate, f-forecast

Chart 2: Exports and manufacturing shipments improving

Year-over-year growth in Alberta exports and manufacturing shipments



Sources: Statistics Canada

Drilling lifts energy investment

Rig activity is picking up in the province. Although drilling remains well below the 5-year average, it started recovering in mid-2016 as oil prices improved. In January 2017, the number of rigs drilling reached the highest level since early 2015. The improvement in activity is expected to carry through 2017 and increase conventional investment by over 20%. In the oil sands, the completion of several large projects in 2017 and cost cutting, which has reduced capital required to sustain existing operations, are expected to pull down investment by almost 7%.

Muted construction outlook

Outside the energy sector, investment continues to be hampered by declining private sector construction spending. Many construction projects underway prior to the oil price drop are winding down. Commercial and industrial spending declined through 2016, dragging down non-residential building construction by almost 8% from 2015. Permit data suggest this weakness will carry into 2017 and outweigh increases in government and institutional spending. On the residential side, housing starts weakened in 2016, falling 34% from 2015. Although wildfire reconstruction activity will lend some support, elevated inventories of multiple unit dwellings and high vacancy rates are expected to keep starts restrained in 2017.

Corporate profits remain weak

Improving oil prices and increased activity will boost corporate profits this year. However, profits were lower-than-expected in 2016 due to weaker economic activity and losses associated with the Wood Buffalo wildfire. The steep decline in profits during the recession means that net operating surplus is forecast to remain well below 2014 levels.

Alberta Household Sector

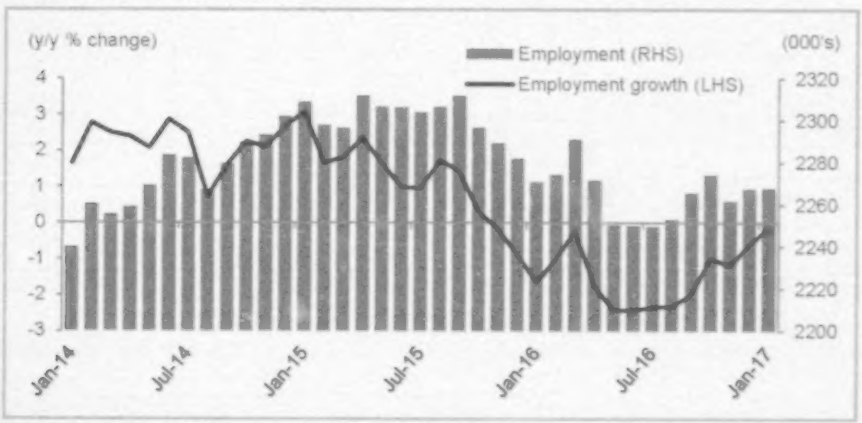
Population growth continues

Alberta's population continues to grow, but at a slower rate. After solid growth of 1.8% in 2016, Alberta's population is forecast to expand by 1.3% in 2017. Strong immigration and natural increase are supporting growth and keeping it above the national average. However, net interprovincial outflows have accelerated in recent quarters and will weigh on growth in 2017.

Labour market adjusting

Signs of improvement have begun to emerge in Alberta's labour market. Employment has increased by almost 18,000 since the low in July 2016 (Chart 3). Employment is expected to post further gains in 2017, growing by 0.9%. The growth will be supported by an improvement in activity in the province and rebuilding efforts in Fort McMurray. The unemployment rate is forecast to come down from current levels to average 8% for the year, but remain elevated as people continue to join the labour force.

Chart 3: Employment shows signs of improvement
Alberta labour market indicators



Source: Statistics Canada

Partial recovery in earnings

Household earnings are expected to improve slightly this year following declines in the past two years. Average weekly earnings (AWE) in the goods sector showed signs of improvement in late 2016, up almost 4% from the low. Service sector earnings remain weak but appear to be stabilizing. AWE are forecast to grow 0.7% this year, down from 1% at *Budget 2016*. The modest gain in earnings will support growth in personal income of 1.8%, following an estimated decline of 3.5% in 2016.

Consumers spending to edge higher

A modest improvement in household incomes and increase in population are expected to support consumer spending. Real spending is forecast to grow by 0.7% in 2017, mainly due to increases on durables, which were hit particularly hard during the recession. Inflation is expected be a modest 1.9%.

Risks to the Outlook

- Lower oil prices remain the main risk to Alberta's recovery. Geopolitical uncertainties, including U.S. trade policy under the new administration and elections in Europe, could dampen global growth and oil demand. Lower compliance by OPEC members and higher-than-expected US production could also lower oil prices.
- Slower population growth due to higher-than-expected out-migration would weigh on consumer spending and housing.
- On the upside, higher oil prices and an acceleration in the construction of approved pipelines could boost business confidence and strengthen Alberta's recovery.

Contact

Catherine Rothrock 780.427.2758